



Australian Fair Pay Commission

Economic and Social Indicators – Monitoring Report

July to December 2008

Released 24 February 2009

Introduction

This is the third issue of the Australian Fair Pay Commission's *Economic and Social Indicators – Monitoring Report*. It is designed to monitor the outcomes from the Commission's minimum wage-setting decisions as well as broader developments in the Australian labour market.

While a focus is placed on the period July to December 2008, many of the indicators are shown over a longer timeframe to provide a broader perspective on how the labour market is performing. This is valuable in the current economic environment, as conditions have fluctuated and expectations about future conditions have become more uncertain. The report also reviews the main results emerging from business surveys on the outlook for the labour market.

As with previous issues, the report has three main sections, broadly reflecting the factors which the Commission must have regard to in fulfilling its wage-setting function. These relate to:

1. macroeconomic developments;
2. employment of low-paid workers; and
3. the safety net and work incentives.

The Commission's third general minimum wage adjustment came into effect in October 2008. This occurred at a time when the labour market was responding to a slowing in both domestic and international economic activity. The transition is ongoing, with employment growth expected to slow further and inflation expected to moderate over the coming year.

It is clear from the various business surveys that the Australian labour market will weaken significantly during the course of 2009. A reduction in working hours can be expected to bear the brunt of the initial adjustment. However, many businesses expect a decline in employment and the rate of unemployment to rise further. The key unanswered question is: how sharp and how prolonged will the weakening of labour market conditions be?

At any point in time, employment growth varies across industries, reflecting factors such as structural change and industry-specific shocks. The labour markets in the more Pay Scale reliant industries have been adjusting in different ways and at different rates.

While employment growth in most industries has moderated over the last six months, and in some cases declined, the balance of the adjustment between hours of employment and the number of people employed has also varied across the industries. Employment in Retail trade and Accommodation, cafes and restaurants has generally been weak over the six months to November 2008.

High inflation outcomes have offset recent increases to the Federal Minimum Wage, leaving its real value broadly unchanged. However, after accounting for the interaction of wages, taxes and transfers, the Commission's modelling suggests that there has been continued improvement to real household disposable income for those households most reliant on a minimum wage-earner.

The Commission welcomes comment on the issues canvassed in this report as input into its 2009 Minimum Wage Review.

A handwritten signature in black ink, reading "Ian R. Harper", followed by a long, sweeping horizontal flourish.

Ian R. Harper
Chairman

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1. Macroeconomic developments

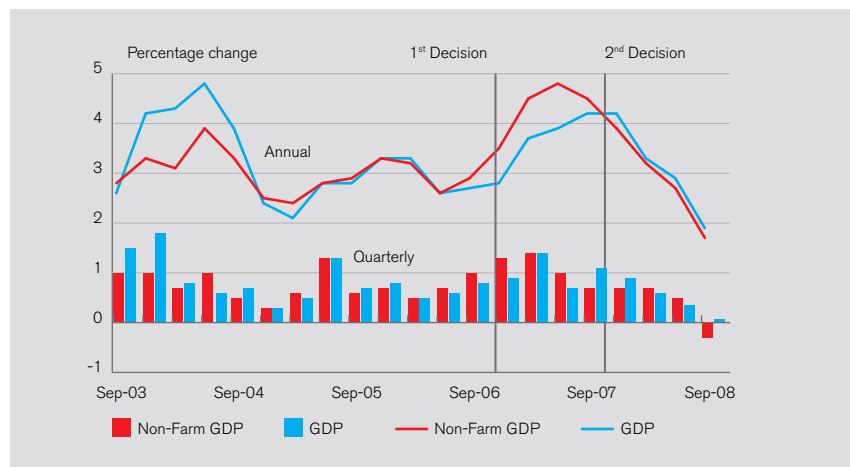
This section focuses on indicators of economic and labour market performance at the aggregate level. Many of the indicators presented, especially employment, lag developments in the broader economy. Some historical data and findings from various business surveys are included to aid the assessment of recent trends.

Economic activity

Economic growth continued to slow from a peak in early 2007, with real non-farm Gross Domestic Product (GDP) growing by 1.7 per cent over the year to the September quarter 2008 (Figure 1). Activity was consistently strong through 2006-07, with growth in non-farm GDP peaking at 4.8 per cent over the year to the June quarter 2007. Since then, growth on a quarterly basis has slowed to rates similar to those achieved in late 2004 and early 2006.

A slowing in economic growth was expected, following tighter monetary policy settings in 2007-08 and significantly weaker external demand. The extent of the slowing that occurred was marked, as illustrated by the 0.3 per cent contraction in non-farm GDP in the September quarter of 2008.

Figure 1: Change in real GDP



Note: All data are seasonally adjusted. The implementation dates for the Commission's general wage-setting decisions are shown for illustrative purposes.

Source: Australian Bureau of Statistics (ABS), *Australian National Accounts: National Income, Expenditure and Product*, September 2008, Catalogue No. 5206.0.

The labour market

The slowing in economic growth has begun to flow through to the labour market. Employment growth peaked at 3 per cent over the year to February 2008 and has since slowed to 1.3 per cent over the year to December 2008, a four-year low (Table 1).

While the number of people employed increased by around 98,000 in the six months to June 2008, employment increased by 35,000 in the following six months, a growth rate of only 0.3 per cent.¹ By comparison, the number of people employed increased by around 153,000 in the six months to December 2007.

Another measure of employment is the total number of hours worked. Over the longer term, the number of people employed and total hours worked increase at similar rates. However, there can be deviations in the two measures of employment in the shorter term, such as when the full-time and part-time composition of employment changes significantly. The total number of hours worked decreased by 0.4 per cent in the six months to December 2008, with a decrease in the average number of hours worked per person.

The number of people in the labour force grew at a slightly higher rate in 2008 than the number of people employed. This produced an increase in the unemployment rate, with the employment-to-population ratio declining by 0.4 percentage points. The changes in unemployment and employment rates over 2008 largely occurred in the second half of the year.

While the unemployment rate increased to 4.5 per cent in December 2008, broader measures suggest that labour underutilisation is around 9 per cent.² The shift towards greater part-time employment in 2008 is likely to have increased underemployment.

¹ The data are in seasonally adjusted terms.

² Centre of Full Employment and Equity (University of Newcastle), *CofFEE Labour Market Indicators*, November 2008; ABS, *Australian Labour Market Statistics*, October 2008, Catalogue No. 6105.0.

Table 1: Selected labour market indicators

	December 2007	June 2008	December 2008	Half-yearly Change Jun to Dec 2008	Annual Change Dec 2007 to Dec 2008
Employment ('000)	10 609	10 707	10 742	0.3%	1.3%
Full-time	7610	7662	7640	-0.3%	0.4%
Part-time	2999	3045	3102	1.9%	3.4%
Hours worked ('000)	350 499	354 941	353 375	-0.4%	0.8%
Unemployment ('000)	466	477	501	5.1%	7.6%
Looking for a full-time job	318	320	349	9.3%	9.9%
Looking for a part-time job	148	157	152	-3.6%	2.7%
Long-term – 1 year or longer	69	68	69	0.2%	-1.1%
Unemployment rate (Per cent)	4.2	4.3	4.5	0.2	0.3
Looking for a full-time job	4.0	4.0	4.4	0.4	0.4
Looking for a part-time job	4.7	4.9	4.7	-0.2	0.0
Participation rate (Per cent)	65.2	65.2	65.0	-0.3	-0.2
Employment to Population (Per cent)	62.4	62.5	62.1	-0.4	-0.4
Labour force ('000)	11 074	11 183	11 243	0.5%	1.5%

Note: All data are seasonally adjusted.

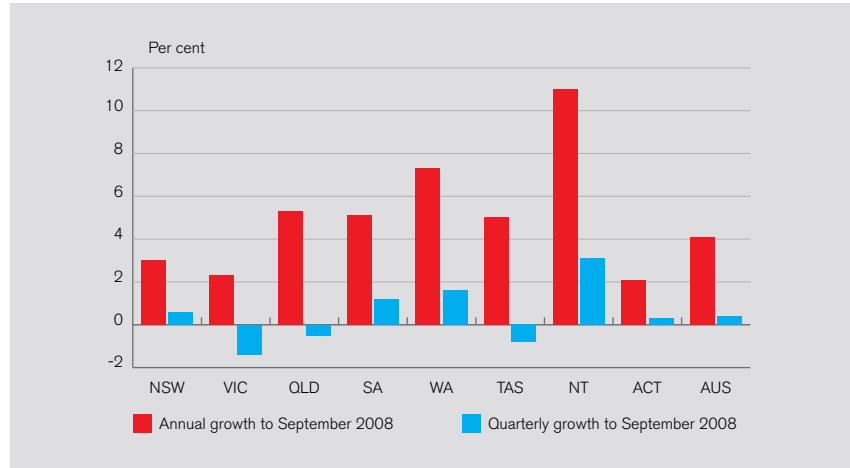
Source: ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001; ABS, *Labour Force, Detailed – Electronic Delivery*, December 2008, Catalogue No. 6291.0.55.001.

Regional labour markets

Patterns of growth in economic activity and employment across the states and territories have changed significantly over the past year, with each region at different stages of the business cycle.

Demand in most state and territory economies grew by over 4 per cent in the year to the September quarter 2008 (Figure 2). However, the two largest states, New South Wales and Victoria, recorded growth of less than 3 per cent. Some states have experienced a sharp turnaround in demand, with the Victorian, Queensland and Tasmanian economies contracting in the September quarter 2008.

Figure 2: Growth in State Final Demand to September 2008

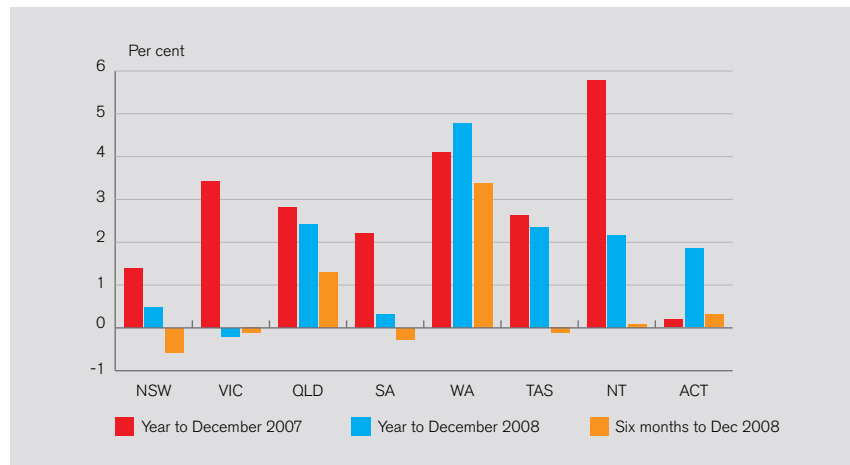


Note: All data are seasonally adjusted. Domestic final demand is reported for Australia.

Source: ABS, *Australian National Accounts: National Income, Expenditure and Product*, September 2008, Catalogue No. 5206.0.

The weakening in economic growth in some states is beginning to show in employment growth. Although Western Australia and Queensland achieved relatively strong employment growth in the six months to December 2008 (Figure 3), employment in New South Wales, Victoria, South Australia and Tasmania declined over the same period.

Figure 3: Employment growth in each state and territory



Note: Data for the states are seasonally adjusted and for the territories are trend.

Source: ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001.

The composition of employment

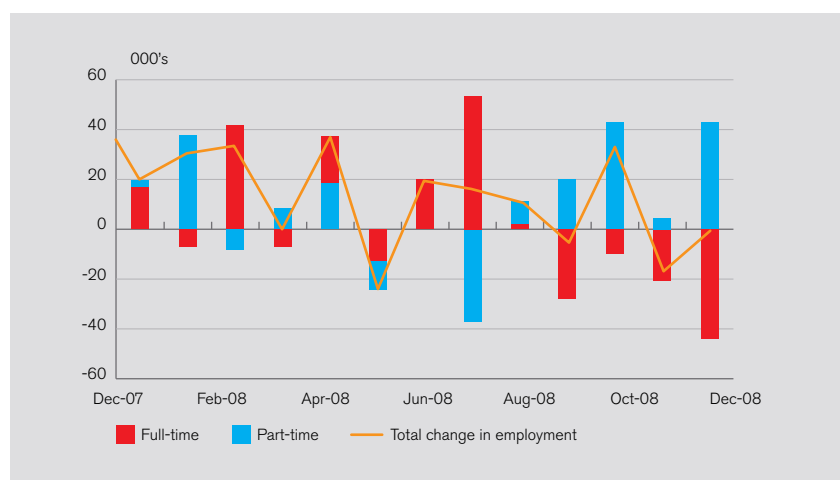
The composition of employment growth changed significantly in the second half of 2008.

Around two-thirds of all new jobs created in 2007-08 were full-time positions: 169,000 full-time compared with 83,000 part-time jobs. This is similar to the aggregate proportion of employees in full-time positions, which is around 70 per cent.

More recently, part-time employment has grown more quickly than full-time employment. Part-time employment increased by 2.1 per cent in the three months to December 2008 and by 3.4 per cent over the year, whereas full-time employment decreased by 0.6 per cent in the three months to December 2008 and increased by 0.4 per cent over the year (Figure 4).

While there is some volatility on a month-to-month basis, the trend over the six months to December 2008 towards part-time job creation is a significant change compared with the year before, when economic growth was stronger. Employers could be using the flexibility of working hours to better tune their workforce structures to an economy growing at a slower rate, rather than effecting major reductions in numbers employed at this stage. Some business surveys confirm this trend. However, a rising proportion of firms have reported reducing the number of their employees.³

Figure 4: Monthly change in full-time and part-time employment



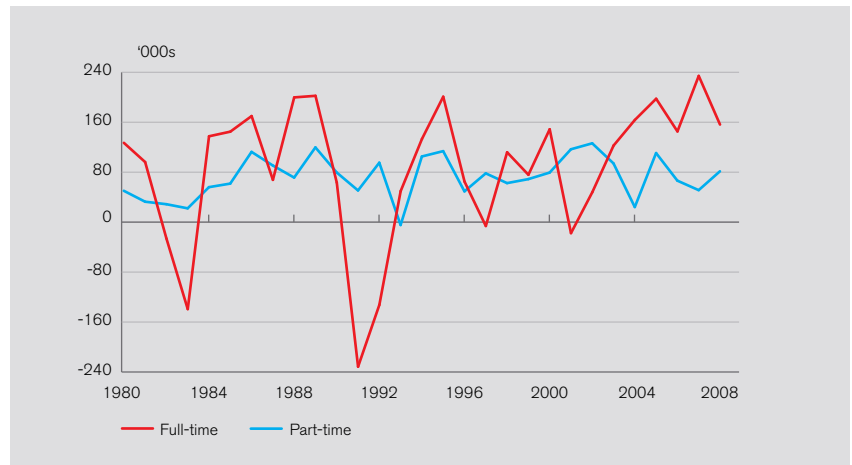
Note: All data are seasonally adjusted.

Source: ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001.

3 For example, the *Commonwealth Bank – ACCI Business Expectations Survey*, February 2009.

Figure 5 provides a long-term perspective on the changes in full-time and part-time employment, particularly through different stages of the business cycle. Most of the change in employment in each quarter has been due to movements in full-time jobs. However, through the various stages of the business cycle, part-time employment has grown at a higher rate than full-time employment and demonstrated fewer, shorter periods of decline. In most of the periods when economic growth was weak, part-time employment continued to grow at moderate rates and partially offset the sharp declines in full-time employment that occurred in the early 1980s, early 1990s and 2001. Part-time employment generally contracted for short periods when full-time employment began to recover.

Figure 5: Annual change in full-time and part-time employment



Note: All data are seasonally adjusted. The figure shows changes in yearly averages for the twelve months to December.
Source: ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001.

Labour market flows

A more detailed understanding of the dynamics of the labour market can be found in data on gross flows between employment, unemployment and non-participation in the labour force.

Table 2 shows the number of people in the working age population who changed their labour force status between successive months. The proportion who changed their status has been generally steady at around 10 per cent per month on average since 2006-07 and this continued over the second half of 2008, when employment growth slowed to a much lower rate.

Table 2: People changing their labour market status between successive months

	Monthly average in the year shown		Average of monthly movements in the quarter shown			
	2006-07	2007-08	September quarter 2008		December quarter 2008	
	Per cent	Per cent	'000	Per cent	'000	Per cent
From full-time employment	2.9	2.9	360	2.6	404	2.9
From part-time employment	3.6	3.7	497	3.6	470	3.4
From unemployment	1.5	1.4	179	1.3	195	1.4
From not in the labour force	2.4	2.4	329	2.4	313	2.3
From all labour force states	10.4	10.4	1364	10.0	1383	10.0

Note: Part-time employment is defined as working 35 hours per week or less. The population used in deriving the gross flows estimates is the Civilian population aged 15 years and over.

Source: ABS, *Labour Force, Detailed – Electronic Delivery*, December 2008, Catalogue No. 6291.0.55.001.

In any given period, some people are becoming unemployed, others are shifting from full-time to part-time work and *vice versa*, while others are leaving or entering the labour force.

Table 3 compares the size of these flows in the June and December quarters of 2008. The data indicate the proportion of the working age population in each labour force state in the first period and the extent to which they changed their status by the next month.

A significant change in the labour market, such as a change in policy or a slowing in economic growth, would be expected to reveal itself in these flows. For example, previous research has found that gross flows into and out of unemployment are cyclical, with both the rate of entry to and exit from unemployment rising as the unemployment rate increases.⁴

The rates of movement between different labour force states, in aggregate and at the more segmented level, were unchanged from the June quarter 2008 to the December quarter. Within this period, employment growth slowed to a much lower rate and the Commission's third general wage-setting decision came into effect.

⁴ R Dixon, J Freebairn and G C Lim, "Time-varying equilibrium rates of unemployment: an analysis with Australian data", *Australian Journal of Labour Economics*, Vol. 10, No. 4, December 2007, pp.205-225.

Table 3: Labour force status in successive months, according to status in initial period, monthly average in the June and December quarters 2008

	Monthly average in the June quarter 2008	Monthly average in the December quarter 2008
	% of Civilian Population	% of Civilian Population
Full-time employment		
Did not change	42.6	43.0
Changed	2.8	2.9
<i>Destinations of those who changed</i>		
<i>part-time employment</i>	2.1	2.1
<i>unemployment</i>	0.2	0.2
<i>not in the labour force</i>	0.5	0.6
Part time employment		
Did not change	15.2	14.9
Changed	3.4	3.4
<i>Destinations of those who change</i>		
<i>full-time employment</i>	2.1	2.1
<i>unemployment</i>	0.2	0.2
<i>not in the labour force</i>	0.9	1.1
Unemployment		
Did not change	1.5	1.4
Changed	1.4	1.4
<i>Destinations of those who changed</i>		
<i>not in the labour force</i>	0.7	0.7
<i>full-time employment</i>	0.3	0.3
<i>part-time employment</i>	0.4	0.4
Not in the Labour Force		
Did not change	30.9	30.6
Changed	2.2	2.3
<i>Destinations of those who changed</i>		
<i>part-time employment</i>	1.1	1.1
<i>unemployment</i>	0.7	0.8
<i>full-time employment</i>	0.4	0.4

Source: ABS, Labour Force, Detailed – Electronic Delivery, December 2008, Catalogue No. 6291.0.55.001.

Wages

Measures of nominal wages have continued to grow steadily over the past six months. The available historical data largely pre-date the increase in the Australian Pay and Classification Scales (Pay Scales) that applied from 1 October 2008.

The Wage Price Index (WPI) increased by 0.9 per cent in the September quarter 2008, to be 4.1 per cent higher over the year (Table 4). This continues the relatively steady trend in the series for the past three years (Figure 6). The average annualised wage increase in federal collective agreements reached in the September quarter 2008 was 4.1 per cent, also little changed over the past six months and compared with outcomes over most of the past five years.

Measures of average weekly earnings grew by 3.5 to 4.7 per cent over the year to the September quarter 2008, with the measures fluctuating between 3 and 5 per cent growth per year since 2006.

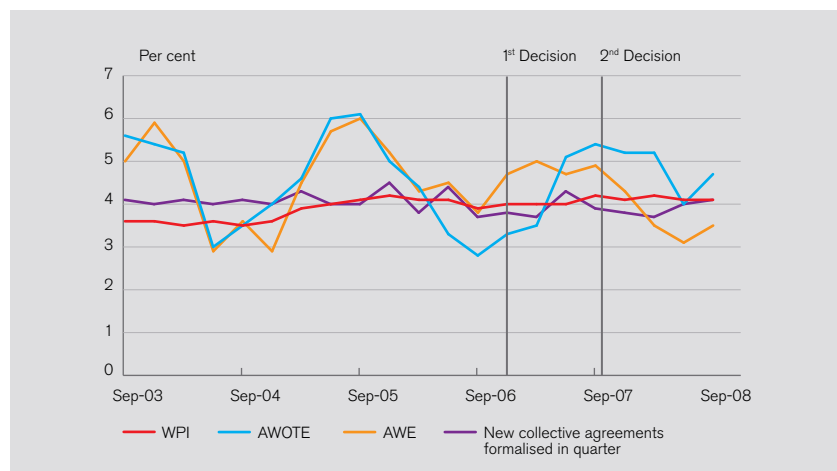
Table 4: Wage growth to the September quarter 2008

	Year to the September quarter 2008	September quarter 2008
	Percentage change	Average annualised percentage change
Wage Price Index (WPI)	4.1	–
Average Weekly Ordinary-Time Earnings (AWOTE) for Full-Time Adult Employees	4.7	–
Average Weekly Earnings (AWE)	3.5	–
New federal collective agreements	–	4.1

Note: WPI, AWOTE and AWE data are seasonally adjusted estimates. AWOTE and AWE are measured at mid-month of quarter.

Source: ABS, *Labour Price Index*, September 2008, Catalogue No. 6345.0; ABS, *Average Weekly Earnings*, August 2008, Catalogue 6302.0; DEEWR, *Trends in Federal Enterprise Bargaining*, September Quarter 2008.

Figure 6: Wage growth, September 2003 to September 2008



Note: WPI, AWOTE and AWE data are seasonally adjusted estimates. AWOTE and AWE are measured at mid-month of quarter.

Source: ABS, *Labour Price Index*, September 2008, Catalogue No. 6345.0; ABS, *Average Weekly Earnings*, August 2008, Catalogue 6302.0; DEEWR, *Trends in Federal Enterprise Bargaining*, September Quarter 2008.

Prices

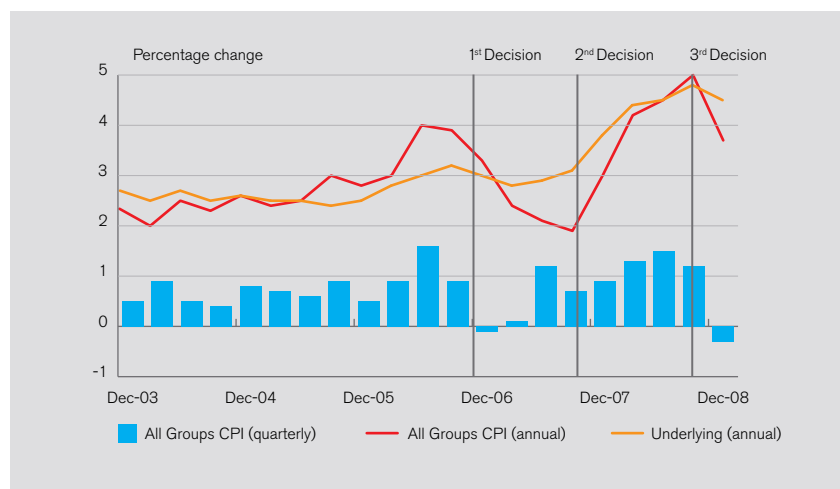
Consumer price inflation peaked in the second half of 2008 but has since begun to slow (Figure 7). The All Groups Consumer Price Index (CPI) fell by 0.3 per cent in the December quarter 2008 to be 3.7 per cent higher over the year. In comparison, the CPI increased by 1.2 per cent in the September quarter 2008 to be 5 per cent higher over the year.

To illustrate the large change in prices during 2008, the CPI increase over the year to the September quarter was the highest increase since 1995, excluding the introduction of the GST. The decrease in the CPI in the December quarter is the largest quarterly fall since the September quarter 1997.

Some of the main components that contributed to the change in consumer prices over the year to the December quarter 2008 were automotive fuel (-4.4 per cent), take-away and fast foods (7 per cent) and rents (8.4 per cent).

The average of the Reserve Bank of Australia's (RBA's) underlying inflation measures remained high, increasing by 0.8 per cent in the December quarter 2008 to be 4.4 per cent higher over the year.

Figure 7: Consumer price inflation



Note: Underlying inflation is the average of the trimmed mean and weighted median inflation measures.

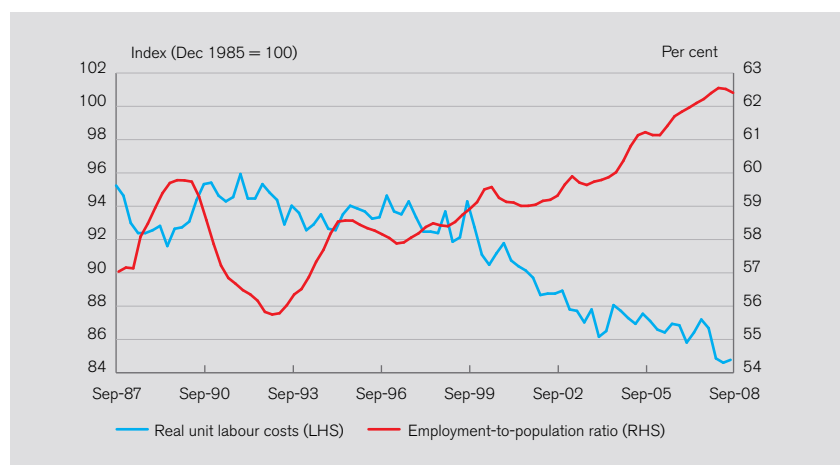
Source: ABS, *Consumer Price Index, Australia*, December 2008, Catalogue No. 6401.0.

Unit labour costs and profitability

While most aggregate wage measures have been reasonably steady over the last three years, labour productivity growth has slowed on a number of measures. GDP per hour worked decreased by 0.3 per cent in the September quarter 2008 and by 0.2 per cent over the year. GDP per hour worked in the market sector decreased by 0.4 per cent in the September quarter 2008, although it increased by 0.2 per cent over the year.

Unit labour costs are part of the link between productivity, employment and profits. Real unit labour costs continued a trend decline over the past three years, declining by 2.9 per cent over the year to the September quarter 2008. There was a steady increase in the employment-to-population ratio over the same period (Figure 8). Although productivity appears to have been weak, the real cost of labour to producers has fallen, making labour more affordable. The ABS has attributed some of the strength in employment growth, above what would be consistent with the economic expansion since 2001, to lower real unit labour costs.⁵

Figure 8: Real unit labour costs and employment-to-population ratio

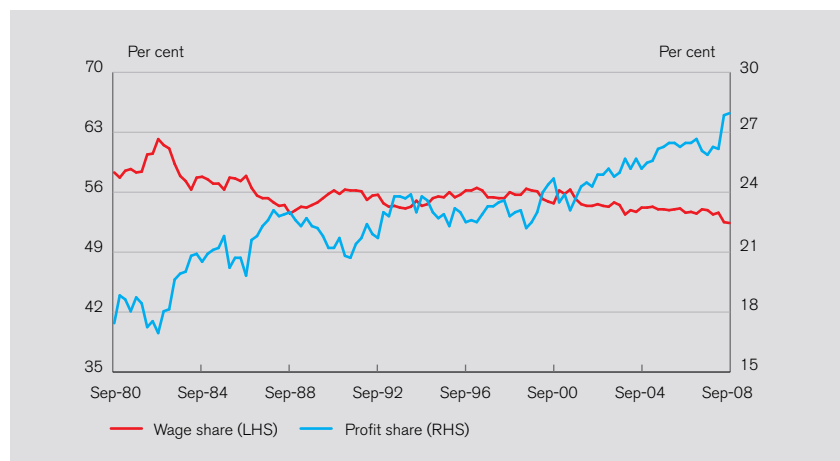


Note: The employment-to-population ratio is the average for the quarter.

Source: ABS, *Australian National Accounts: National Income, Expenditure and Product*, September 2008, Catalogue No. 5206.0; ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001.

Over the past two years, the profit share of total factor income has been steady at a record high of between 26 and 27 per cent of national income, while the wage share has been broadly steady at around 53 per cent. However, the profit share increased in mid-2008, to a high of 28 per cent (Figure 9). Correspondingly, the wage share of total factor income declined by 1.1 percentage points to 52.4 per cent.

⁵ ABS, *Australian National Accounts: National Income, Expenditure and Product*, June 2005, 'Feature article 1: The relationship between GDP and employment', Catalogue No. 5206.0, based on an analysis of quarterly growth rates.

Figure 9: Wage and profit shares of national income

Note: The profit share is calculated as the gross operating surplus of corporations as a share of total factor income. The wage share is calculated as the total compensation of employees as a share of total factor income.

Source: ABS, *Australian National Accounts: National Income, Expenditure and Product*, September 2008, Catalogue No. 5206.0.

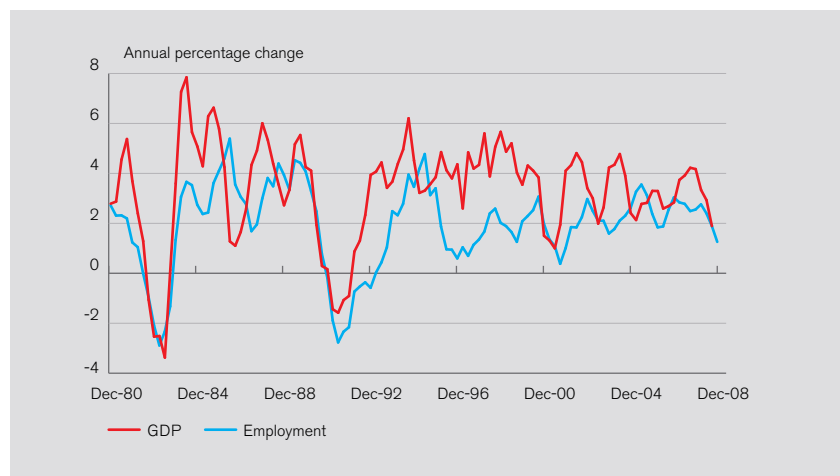
Gross operating profits increased by 31.3 per cent over the year to the September quarter 2008. Profits increased at a slower rate in the September quarter, by 5.2 per cent, compared to 15.7 per cent in the previous quarter. These fluctuations have largely been driven by profits in the mining industry. However, other industries showed similar patterns in profit growth over the year.

Economic activity and employment over the longer term

Changes to employment growth typically follow changes in economic growth. The speed at which changes in economic activity are reflected in changes in employment can vary. In particular, a decline in employment growth quickly follows a sharp fall in economic activity as occurred in the late 1980s and early 1990s (Figure 10). On this basis, a further slowing in employment growth would be expected in 2009.

The ABS suggests that the lag in employment growth from peaks in economic growth is around two to four quarters in length, based on recent history.⁶

⁶ ABS, *Australian National Accounts: National Income, Expenditure and Product*, June 2005, 'Feature article 1: The relationship between GDP and employment', Catalogue No. 5206.0, based on an analysis of quarterly growth rates.

Figure 10: Employment and GDP, annual growth rates

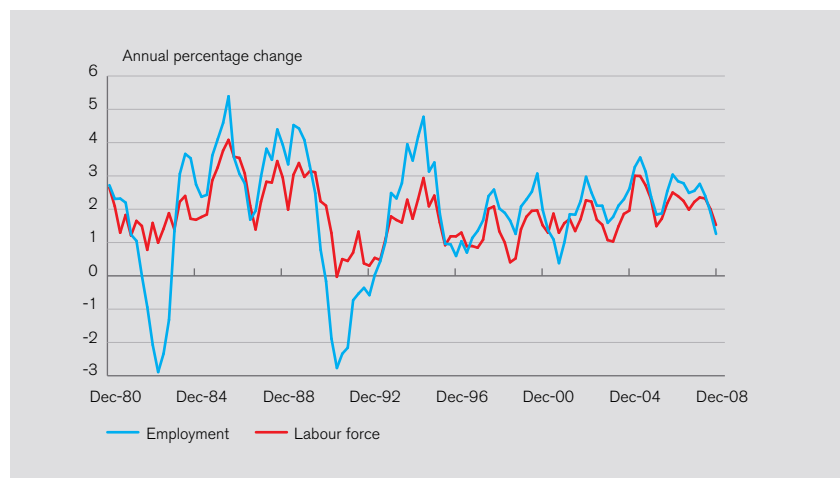
Note: Data are in trend terms. Employment data are based on the average for the quarter.

Source: ABS, *Australian National Accounts: National Income, Expenditure and Product*, September 2008, Catalogue No. 5206.0; ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001.

Generally, the labour force grows at a stronger rate if employment growth is stronger, a so-called “encouraged worker” effect. As a result, changes to the unemployment rate generally occur slowly. For example, between 2004 and 2006, increases in employment were met by rising labour force participation (Figure 11). This suggests that job prospects and work incentives combined to attract an increasing number of people into the labour force to meet demand. At times, employment has grown at markedly higher or lower rates than the labour force and this has produced large changes in the unemployment rate.

Employment growth must exceed labour force growth for there to be a fall in the unemployment rate. Over the six months to December 2008, employment increased by 0.3 per cent and the labour force increased by 0.5 per cent, resulting in a 0.2 percentage point increase in the unemployment rate.

Figure 11: Employment and labour force growth



Note: All data are seasonally adjusted.

Source: ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001; ABS, *Labour Force, Detailed – Electronic Delivery*, December 2008, Catalogue No. 6291.0.55.001.

The economic and labour market outlook

Domestic economic growth forecasts have generally been revised downwards since the Commission's 2008 general Wage Setting Decision was announced. This has been in reaction to a sudden deterioration in the global economic environment, which has also seen macroeconomic policy settings loosened.

In its *Updated Economic and Fiscal Outlook*, published in February 2009, the Australian Government revised its forecast for economic growth in 2008-09 to 1 per cent, compared with 2¾ per cent at the time of the 2008-09 Budget in May (Table 5).

The Government noted that the world economy has deteriorated sharply since the *Mid-Year Economic and Fiscal Outlook*, with a global recession now expected in 2009. Very substantial fiscal and monetary policy responses are considered to be only partially able to offset the impact of the global recession.⁷

Forecasts of employment growth have also been reduced, consistent with slower economic growth. The Government expects employment to contract through 2009 and remain weak in 2010, with the unemployment rate rising to 7 per cent by June 2010.

⁷ Australian Government, *Updated Economic and Fiscal Outlook*, February 2009, p.27.

Table 5: Australian Government domestic economic forecasts

	2007-08 Outcomes	2008-09 Budget Forecasts	2008-09 UEFO Forecasts	2009-10 UEFO Forecasts
	Per cent	Per cent	Per cent	Per cent
Gross Domestic Product	3.7	2¾	1	¾
Non-farm product	3.6	2¼	1	½
Labour Market				
Employment	2.5	¾	-¼	0
Unemployment rate	4.3	4¾	5½	7
Prices and Wages				
Consumer Price Index	4.5	3¼	2	2
Wage Price Index	4.1	4¼	3¾	3¼

Note: Figures for Gross Domestic Product are year average percentage changes. Figures for Employment, Consumer Price Index and Wage Price Index are over-the-year. Unemployment rates are for the June quarter.

Source: Australian Government, *Mid-Year Economic and Fiscal Outlook 2008-09*, released November 2008; and Australian Government, *Updated Economic and Fiscal Outlook*, February 2009.

The Government also expects inflation to fall from its current high levels. It has lowered its forecasts for CPI inflation to 2 per cent in 2008-09 and 2009-10. Inflationary pressures are expected to ease due to weaker global growth and domestic demand, moderating wage pressures and lower oil prices.

Similarly, the RBA has revised its forecasts for inflation downwards since 2008.⁸ Price pressures are expected to ease as the slowing in activity alleviates capacity pressures and reduces the pricing power of businesses (Table 6). The RBA forecasts employment to fall over 2009, although growth is expected to resume as the economy gradually recovers.

Table 6: RBA inflation forecasts

	Percentage change over the year to the quarter shown				
	September 2008	December 2008	June 2009	December 2009	June 2010
Consumer price index	5.0	3.7	1¾	2½	2¾
Underlying inflation	4.7	4.3	3½	3	2¾

Note: Underlying inflation is the average of the trimmed mean and weighted median inflation measures. Forecasts are based on December quarter 2008 figures.

Source: RBA, *Statement on Monetary Policy*, February 2009.

Private sector forecasts for key economic and labour market indicators range widely, suggesting considerable uncertainty over the outlook. A survey of 18 private sector economists in early 2009 found economic growth forecasts for 2009 ranging from 0.2 per cent to 1.6 per cent, with each respondent expecting an improvement in growth in the following year.⁹ Most respondents expected the unemployment rate to increase to 6 per cent in 2009, with some expecting a much higher rate.

⁸ RBA, *Statement on Monetary Policy*, February 2009, pp. 64-67.

⁹ Consensus Economics, *Asia Pacific Consensus Forecasts*, January 12, 2009.

Various forward-looking surveys point to a weakening in business conditions, profitability and employment intentions, with the levels of some indicators comparable with previous periods when there was a sharp increase in unemployment. These findings are generally consistent across industries and for different firm sizes.

A further slowing in activity is expected by employers over the next quarter to a year. For example, the National Australia Bank Monthly Business Survey indicated that, while business conditions and confidence improved slightly in December 2008, they are at levels comparable with previous periods of weak economic activity, such as in the early 1990s.¹⁰

The NAB survey and the *Commonwealth Bank – ACCI Business Expectations Survey* are representative of the findings emerging from a range of business surveys across a wide range of indicators.¹¹ The surveys found that the demand for labour weakened considerably in the December quarter 2008 and into 2009. This was driven by a decline in actual employment and expectations of a fall in employment in the next quarter, in terms of both people employed and the extent of overtime. However, after an extended period of an historically tight labour market, the data are consistent with the view that many businesses will hoard labour during the slowdown in economic activity.

The *Manpower Employment Outlook Survey* for the first quarter of 2009 indicated that employment expectations have declined and that employers are expressing 'cautiously optimistic hiring intentions'.¹² Employers are reporting weaker hiring prospects in all industries compared with hiring prospects a year ago. Fewer employers predicted an increase in total employment than for each of the four surveys conducted in 2008, while more employers predicted a decrease in total employment.

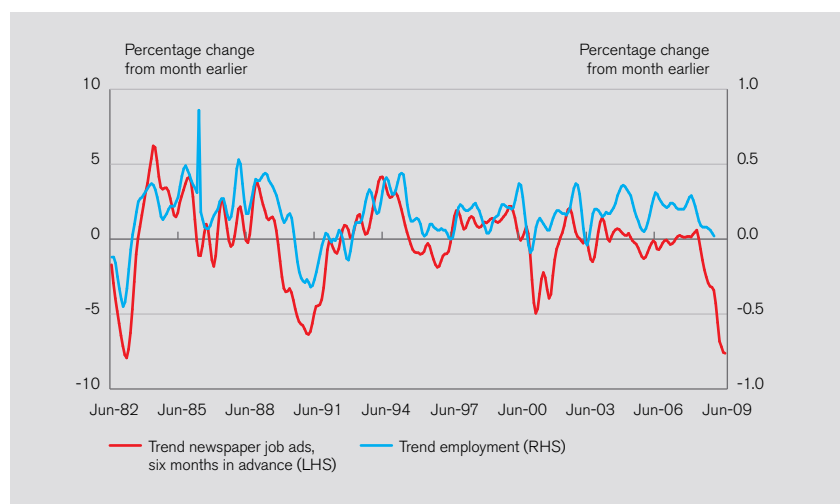
Various measures have shown a significant decline in the number of job vacancies. The ANZ Bank reported a sharp fall in job advertisements over the December quarter 2008 (Figure 12). The total number of job advertisements decreased by 23.4 per cent in trend terms over the year. Based on historical relationships between employment and the job vacancies series, employment should decline further in the first half of 2009.

10 National Australia Bank, *Monthly Business Survey and Economic Outlook*, December 2008.

11 *Commonwealth Bank – ACCI Business Expectations Survey*, February 2009.

12 Manpower, *Manpower Employment Outlook Survey Australia Q1./09*.

Figure 12: Monthly trend growth in newspaper job advertisements and employment



Note: The trend in newspaper job advertisements is a forward-looking indicator of employment and ends at June 2009.

Source: ANZ Bank, *Job Advertisements Series*, December 2008; ABS, *Labour Force Spreadsheets*, December 2008, Catalogue No. 6202.0.55.001.

While the business surveys indicate similar readings for economic conditions and labour market developments in 2009, they offer mixed views on the outlook for selling prices. Some surveys report that selling prices are expected to increase in 2009 at similar high rates to those in 2008, due to higher import costs and the desire to offset expected losses in sales revenue and profits.¹³ However, other surveys point to a fall in price expectations, as demand slows.¹⁴ Wages are generally expected to grow at a slower rate in 2009, consistent with less demand and greater availability of labour.

Summary

The economic outlook has weakened more quickly than was anticipated in mid-2008. While economic activity, employment and inflation were expected to slow somewhat over the next couple of years, the extent of the slowing in activity and employment is now expected to be greater. From relatively high levels, the headline rate of inflation is now expected to fall quickly, although the depreciation of the Australian dollar will offset the disinflationary pressures of a slowing economy.

It is clear from the various business surveys that the Australian labour market will weaken significantly during the course of 2009. A reduction in working hours can be expected to bear the brunt of the initial adjustment. However, more businesses expect a decline in employment and it now seems inevitable that the unemployment rate will rise. The key unknown is how sharp and how prolonged the weakening of labour market will be.

¹³ Australian Industry Group and Deloitte, *National CEO Survey*, January 2009.

¹⁴ Australian Chamber of Commerce and Industry, *ACCI Survey of Investor Confidence*, January 2009.

2. Employment of low-paid workers

This section focuses on employment outcomes for low-skilled workers as well as employment in industries and occupations most reliant on Pay Scales.

Selected demographic groups

Table 7 shows the employment rates for a selection of demographic groups with a high concentration of low-skilled workers. It shows that following the Commission's third wage-setting decision, part-time employment rates increased and full-time employment rates decreased for each of these groups. This shift was also evident in the aggregate labour market, as shown in the previous chapter. The largest fall in the total employment rate was for 20-24 year olds who are not in full-time education.

Table 7: Percentage of people in the selected groups who are in employment

	Average Monthly Percentage			
	Before and after second decision (October 2007)		Before and after third decision (October 2008)	
	July 2007 to September 2007	October 2007 to December 2007	July 2008 to September 2008	October 2008 to December 2008
<i>Percentage of unmarried individuals living in non-metro areas:</i>				
in full-time employment	34.7	34.1	34.6	34.2
in part-time employment	18.6	18.2	17.7	18.3
<i>Percentage of 20-24 year olds who are not in full-time education:</i>				
in full-time employment	69.7	70.3	68.9	66.6
in part-time employment	13.9	13.4	14.6	15.2
<i>Percentage of migrants from non-English speaking backgrounds:</i>				
in full-time employment	38.9	39.3	39.2	39.0
in part-time employment	14.2	14.5	15.1	15.2
<i>Percentage of single parents:</i>				
in full-time employment	32.4	32.7	34.0	32.7
in part-time employment	22.7	22.7	21.2	22.3
<i>Percentage of non-dependent children:</i>				
in full-time employment	62.3	61.8	62.0	61.8
in part-time employment	17.0	16.3	16.1	16.4
Percentage of civilian population:				
in full-time employment	44.5	44.8	44.8	44.4
in part-time employment	17.7	17.6	17.6	17.8

Note: Average monthly percentages are shown. All data seasonally adjusted.

Source: ABS, *Labour Force, Detailed – Electronic Delivery*, December 2008, Catalogue No. 6291.0.55.001.

Employment by industry and occupation categories

Table 8 provides an overview of employment in low-skilled industries and occupations in the year to November 2008 and over the last ten years.¹⁵

Since November 1998, the number of employees and hours worked in Accommodation, cafes and restaurants and Retail trade has generally grown at or above the average for all employees. However, employment in these industries can be highly variable in the short term. The number of employees and hours worked in Retail trade declined over the year to November 2008, while employment grew at a much stronger rate in Accommodation, cafes and restaurants than for the labour market as a whole.

Both the number of Elementary clerical, sales and service workers and the hours they worked declined over the year to November 2008, while for Labourers and related workers employment grew strongly. Unlike all employees in the more low-skilled industries, the number of employees in these occupations has grown at a much lower rate than for all employees over the period since November 1998.

Around 40 per cent of Retail trade workers are classified as Elementary clerical, sales and service workers. Therefore, changes in employment in those occupations are likely to reflect to a large degree in Retail trade. In contrast, Labourers and related workers are employed more evenly across industries.

Table 8: Growth in the number of employees and hours worked by industry and occupation

	Percentage change in the year to November 2008		Annualised percentage change since November 1998	
	Employees	Hours	Employees	Hours
<i>Industries</i>				
Accommodation, cafes and restaurants	7.1	4.9	2.9	2.9
Retail trade	-2.2	-3.9	2.7	2.5
<i>Occupations</i>				
Elementary clerical, sales and service workers	-0.2	-1.2	0.9	0.6
Labourers and related workers	5.2	5.2	0.6	0.9
All employees	2.1	1.4	2.7	2.5

Source: ABS, *Labour Force, Detailed, Quarterly*, November 2008, Catalogue No. 6291.0.55.003.

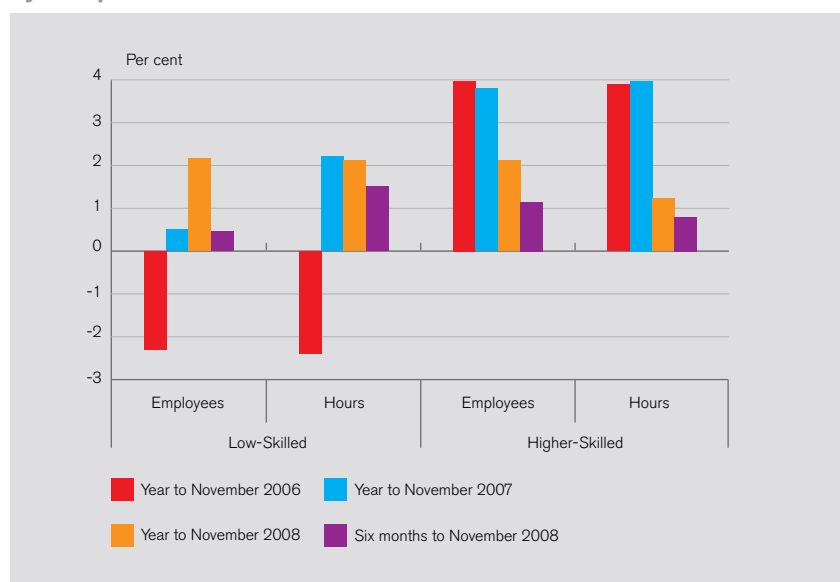
Recent data on employment growth by occupation are illustrated in Figure 13. In 2006, there was a marked difference in employment outcomes between low-skilled and higher-skilled employees. The number of employees and hours worked in low-skilled occupations both decreased by over 2 per cent, while the number of employees and hours worked in higher-skilled occupations both increased by almost 4 per cent.

¹⁵ At this disaggregated level, the estimates of employment are subject to greater error and make analysis over the short to medium terms more challenging.

Over the year to November 2008, the number of employees in low-skilled occupations increased by 2.2 per cent compared with an increase of 2.1 per cent for higher-skilled employees. Some of the slowing in employment growth for higher-skilled workers can be attributed to the recent weaker economic conditions facing industries that tend to employ higher-skilled workers, with skilled job vacancies significantly lower than they were a year ago.¹⁶

However, over the six months to November 2008, growth in the number of employees in low-skilled occupations has slowed significantly, to around 0.5 per cent, with the average number of hours of employment increasing at a higher rate.

Figure 13: Growth in number of employees and hours worked by occupation skill level



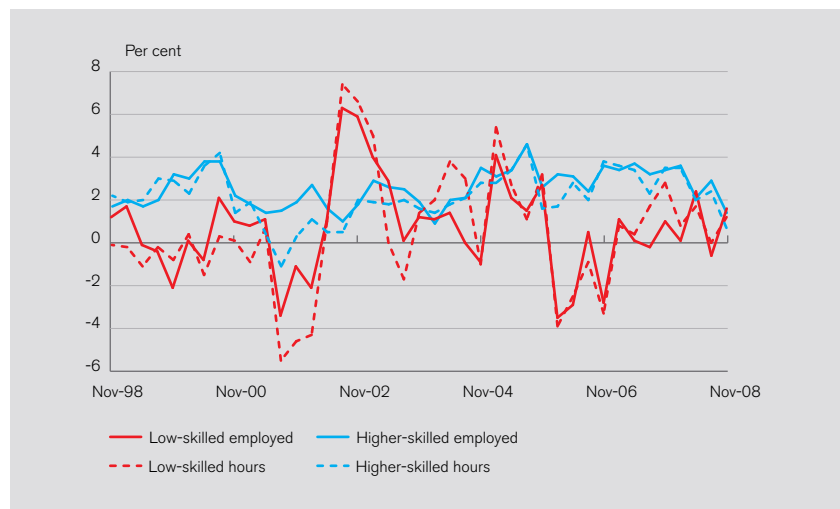
Note: Data seasonally adjusted by AFPCS. Low-skilled occupations include Elementary clerical, sales and service workers and Labourers and related workers.

Source: ABS, *Labour Force, Detailed, Quarterly*, November 2008, Catalogue No. 6291.0.55.003.

Figure 14 illustrates these trends over the ten-year period since 1998. Employment in low-skilled occupations has grown at a more variable but slower rate on average than in the higher-skilled occupations, where employment appears to follow the business cycle.

¹⁶ Australian Department of Education, Employment and Workplace Relations, *Vacancy Report*, January 2009

Figure 14: Growth in employment and hours worked in low-skilled occupations versus higher-skilled occupations, 1998 to 2008



Note: Annual growth rates for each quarter are shown. Data seasonally adjusted by AFPCS. Low-skilled occupations include Elementary clerical, sales and service workers and Labourers and related workers.

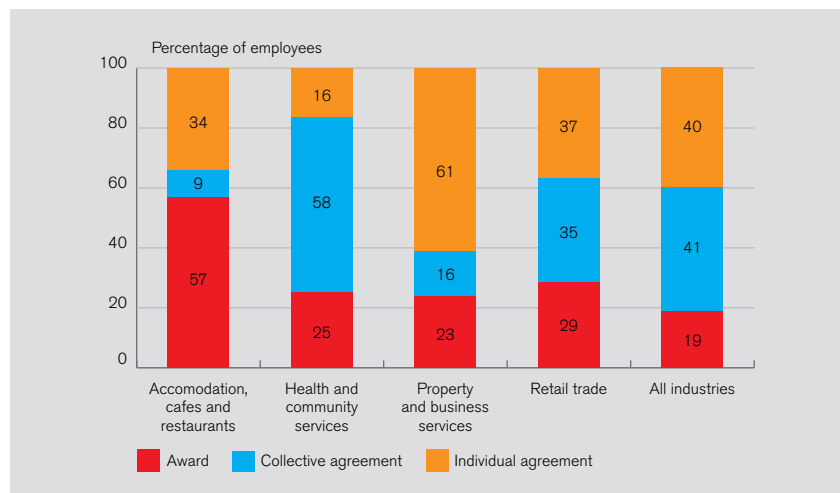
Source: ABS, *Labour Force, Detailed, Quarterly*, November 2008, Catalogue No. 6291.0.55.003.

Employment in selected industries

This section focuses on employment in the four industries that are estimated to account for around 70 per cent of all Pay Scale reliant employees – Accommodation, cafes and restaurants; Health and community services; Property and business services; and Retail trade.

Research undertaken by ACIL Tasman¹⁷ highlights some differences and similarities among industries that are most reliant on Pay Scales in the Australian labour market. This helps to understand how different industries and their labour markets respond to changes in the economy. For example, the incidence of Pay Scale reliance varies significantly across these four industries, from 57 per cent of employees in Accommodation, cafes and restaurants to 23 per cent in Property and business services (Figure 15).

¹⁷ ACIL Tasman, *A Profile of the Accommodation, cafes and restaurants industry*, report commissioned by the Australian Fair Pay Commission, September 2008; ACIL Tasman, *A Profile of the Health and Community Services industry*, report commissioned by the Australian Fair Pay Commission, September 2008.

Figure 15: Pay-setting methods across industries

Source: ABS, *Employee Earnings and Hours, Australia*, May 2006, Catalogue No. 6306.0.

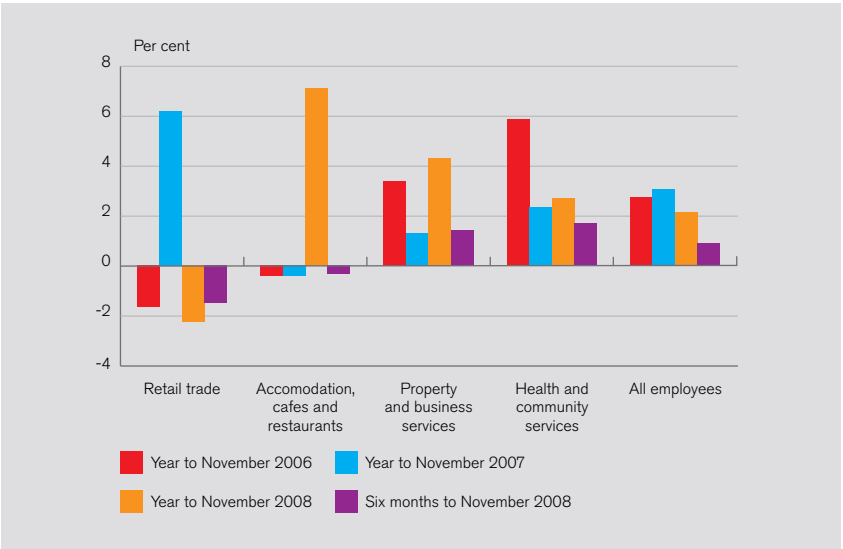
Figure 16 indicates the different employment outcomes for each of these industries. Growth in the number of employees in Property and business services and Health and community services has generally been above that for all employees. In contrast, growth in the number of employees in Retail trade and Accommodation, cafes and restaurants has generally been below that for all employees.

The different trends across these industries are still evident in their growth rates in the six months to November 2008. The number of employees in Retail trade and Accommodation, cafes and restaurants declined over the six months to November 2008 and increased in Property and business services and Health and community services.

However, Figure 16 also illustrates the volatility of employment estimates by industry. Both Retail trade (in the year to November 2007) and Accommodation, cafes and restaurants (in the year to November 2008) had a period of particularly strong employment growth. By comparison, employee growth in Health and community services has grown at a more stable rate.

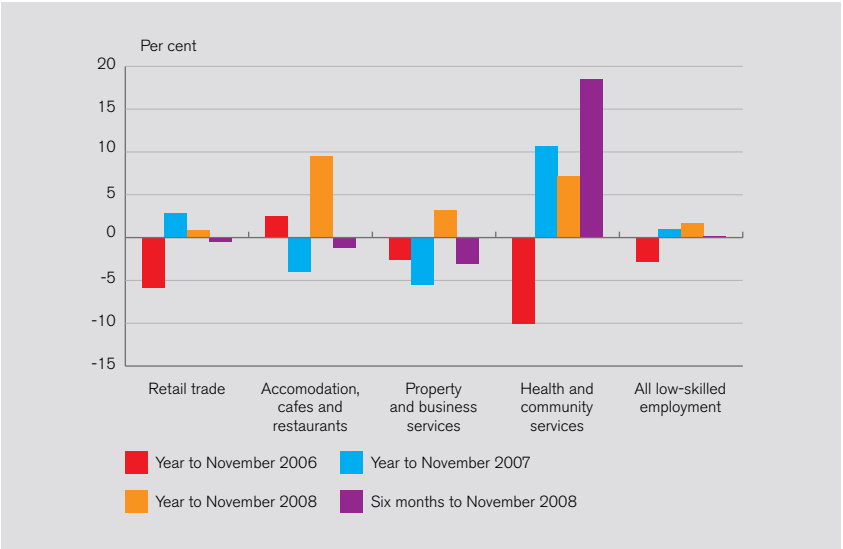
A comparison of low-skilled workers in the selected industries is shown in Figure 17. Low-skilled employment has been growing strongly in Health and community services over the two years to November 2008. However, low-skilled employment in Retail trade, Accommodation, cafes and restaurants and Property and business services has declined in the six months to November 2008.

Figure 16: Growth in number of employees by industry



Note: Data seasonally adjusted by AFPCS.
Source: ABS, *Labour Force, Detailed, Quarterly*, November 2008, Catalogue No. 6291.0.55.003.

Figure 17: Growth in low-skilled employment by industry



Note: Data is unavailable for low-skilled employees by industry. This figure uses total employment which also includes employers, own account workers and contributing family workers. Low-skilled occupations include Elementary clerical, sales and service workers and Labourers and related workers. Data seasonally adjusted by AFPCS.
Source: ABS, *Labour Force, Detailed, Quarterly*, November 2008, Catalogue No. 6291.0.55.003.

Wage growth in selected industries and occupations

Table 9 compares the change in wages across selected industries and occupations. Average wages in Accommodation, cafes and restaurants grew at a significantly lower rate in the September quarter 2008 than in Retail trade and all industries. Generally, wage growth has been lower for low-skilled occupations than higher-skilled occupations.

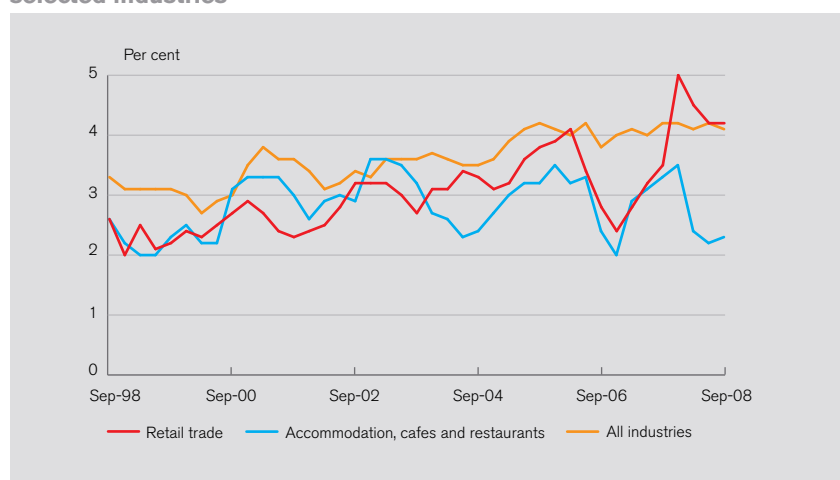
Table 9: Growth in total hourly rates of pay, excluding bonuses, in selected industries and occupations

	Growth in the year to the September quarter 2008	Average annual growth in the ten years to the September quarter 2008
	Percentage change	Percentage change
<i>Industries</i>		
Accommodation, cafes and restaurants	2.3	2.8
Retail trade	4.2	3.1
<i>Occupations</i>		
Elementary clerical, sales and service workers	3.5	3.2
Labourers and related workers	3.4	3.4
Intermediate clerical, sales and service workers	3.2	3.4
All industries/occupations	4.1	3.7

Source: ABS, *Labour Price Index*, September 2008, Catalogue No. 6345.0.

Over the ten years to the September quarter 2008, average wages in Accommodation, cafes and restaurants and Retail trade have grown more slowly than the average across all industries (Figure 18). There has been some year-to-year volatility for each industry. Wage growth appeared to slow in the two industries since mid-2008, whereas aggregate wage growth remained steady.

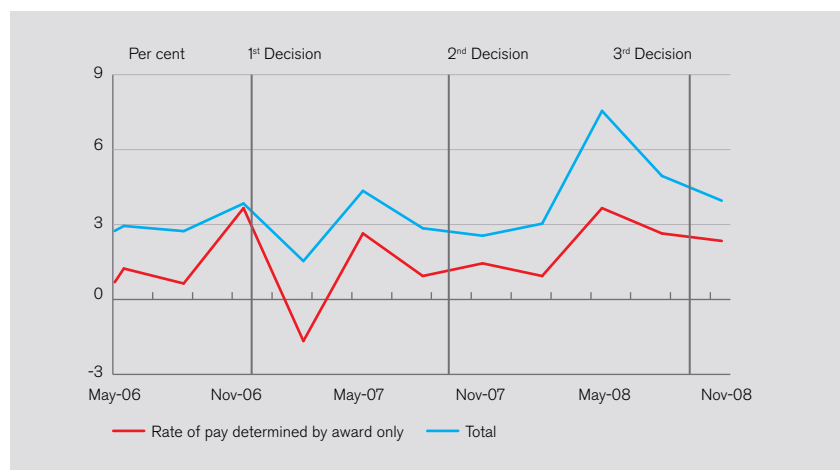
Figure 18: Annual growth in total hourly rates of pay, excluding bonuses, selected industries



Source: ABS, *Labour Price Index*, September 2008, Catalogue No. 6345.0.

The Melbourne Institute Wages Report found that wages for the lowest-paid employees have been growing more slowly than for the labour force as a whole (Figure 19). Since mid-2006, average annual growth in the total wage rate for employees whose pay is determined solely by an award has generally been lower than that of average wages.

Figure 19: Average annual growth in total wage rate by pay-setting method



Note: The basic hourly wage rate was used in the previous *Economic and Social Indicators – Monitoring Report*, however this series has been discontinued by the Melbourne Institute.

Source: Melbourne Institute of Applied Economic and Social Research, *Melbourne Institute Wages Report*, November 2008.

Summary

The recent economic weakness is beginning to affect some of the more Pay Scale reliant industries and occupations.

Employment growth in some of the more Pay Scale reliant industries, such as Retail trade and Accommodation, cafes and restaurants, has been volatile over the last two years. However, employment growth has been particularly low in the six months to November 2008 in those two industries.

Of the low-skilled occupations, employment for Elementary clerical, sales and service workers declined over the past year, while employment for Labourers and related workers grew more strongly than for all occupations.

3. The safety net and work incentives

This section presents indicators of the real and relative value of selected Pay Scales, as well as work incentives and living standards for different household types and employees.

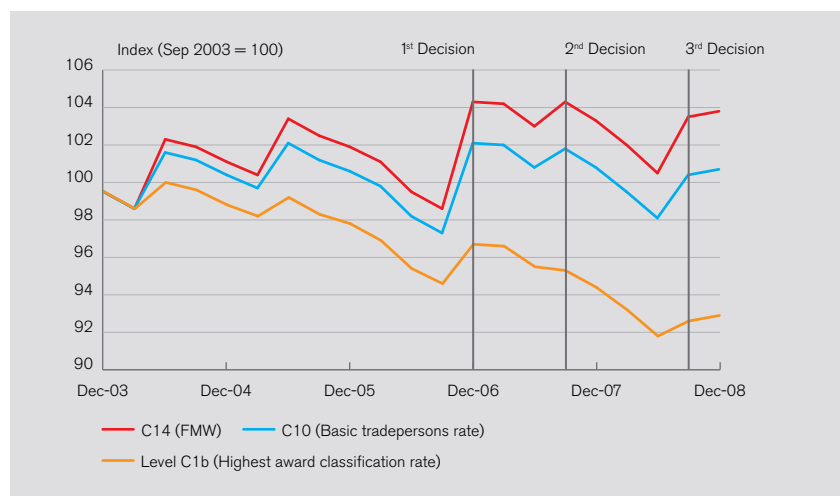
Relative and real values of selected Pay Scales

Estimates of the value of Pay Scales adjusted for price inflation can reflect the extent of the safety net provided by minimum wages, the strength of work incentives and the incentive to enter wage bargaining rather than rely on minimum wages.

The real value of the Federal Minimum Wage (FMW) has been broadly unchanged over the two years to December 2008 (Figure 20). The increase in the standard FMW on 1 October 2008 was 4.1 per cent, slightly below the change in the CPI over the period since the Commission's 2007 general Wage-Setting Decision. The real value of the basic tradesperson's rate has declined by around 2 per cent over the same period.

There has been a gradual decline in the FMW relative to various measures of earnings over the same period (Figure 21).

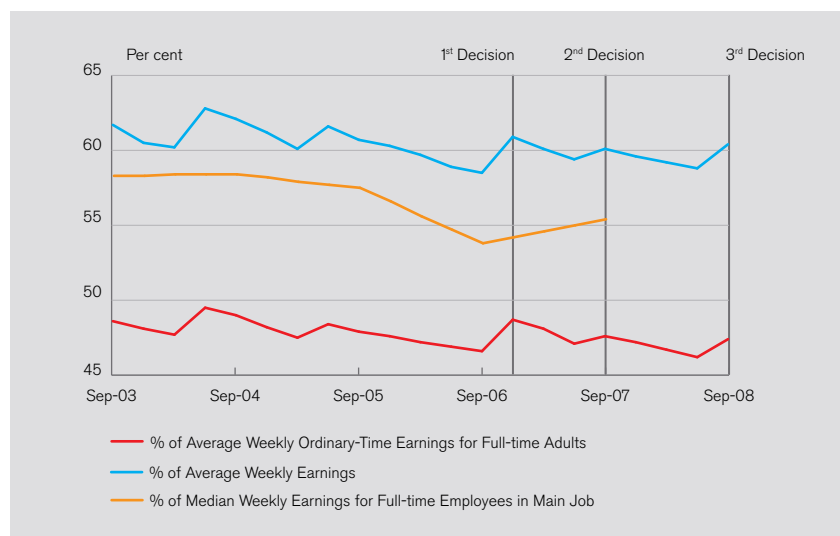
Figure 20: Trend in the real value of selected Pay Scales



Note: Pay Scale rates are measured at end of quarter, except for the September quarter 2007 and 2008 which measures the Pay Scale rates as of 1 October.

Source: ABS, *Consumer Price Index, Australia*, December 2008, Catalogue No. 6401.0; Metal, Engineering and Associated Industries Award 1998.

Figure 21: The FMW relative to average and median earnings



Note: Pay Scale rates are measured at end of quarter, except for the September quarter 2007 and 2008, which measures the Pay Scale rates as of 1 October. AWOTE and AWE are measured at mid-month of the quarter. The next release of data on median weekly earnings for full-time employees in main job is in April 2009.

Source: ABS, *Average Weekly Earnings*, August 2008, Catalogue No. 6302.0; ABS, *Employee Earnings Benefits and Trade Union Membership*, August 2007, Catalogue No. 6310.0.

Real disposable incomes

The income safety net of low-paid workers is determined by the net result of the interaction of wages, taxes and transfers. Changes to tax and/or transfer parameters, along with wage increases, will have varying effects on the value of this safety net depending on household size and composition.

Relevant changes that occurred during 2008 include:

- The FMW increased by \$21.66 per week on 1 October, a 4.1 per cent increase;
- Social security payments were indexed on 20 March and 20 September, based on the CPI figures for the December quarter 2007 and June quarter 2008, respectively; and
- Changes were made to the tax-transfer system in the 2008-09 Australian Government Budget. These included:
 - personal income tax cuts, which will be introduced over four years;
 - the 30 per cent income tax threshold was increased from \$30,001 to \$34,001 and the Low Income Tax Offset was increased from \$750 to \$1,200;
 - the Child Care Tax Rebate was increased from 30 to 50 per cent and is now paid quarterly; and
 - the thresholds for the Medicare Levy Surcharge were increased.

In its monitoring of the value of the safety net, the Commission focuses primarily on changes in the situation of households most reliant on the income safety net—that is, households with one earner on the standard FMW. Changes in the real value (adjusted for CPI inflation) of disposable incomes are tracked over time¹⁸ for five different household types with one person on the FMW: (i) a single person without children; (ii) a couple without children; (iii) a single-parent pensioner with one child aged 5 to 7;¹⁹ (iv) a single-parent allowee with a child aged 8 to 12 and (v) a couple with two children aged 5 to 12.

Over the period from August 2005 to November 2008, the disposable incomes of all the households that were modelled increased in real terms (Figure 22). The approximate real increases for each of the household types over this period were as follows:

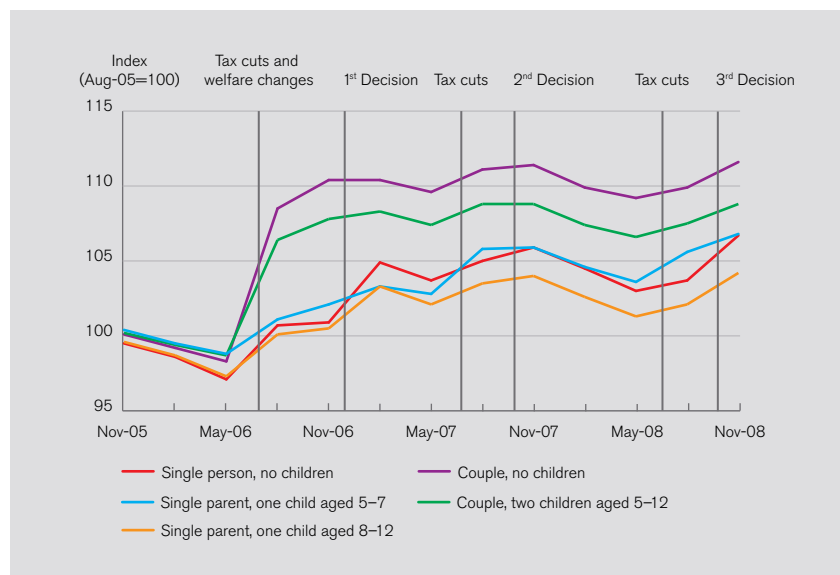
- 12 per cent for a couple without children;
- 9 per cent for a couple with two children aged 5 to 12;
- 7 per cent for a single-parent pensioner household and a single person without children; and
- 4 per cent for a single-parent allowee with a child aged 8 to 12.

All the household types that were modelled benefited from the tax cuts in July 2008 and the minimum wage increase in October 2008. The single-parent pensioner gained most from the tax cuts, experiencing a 2 per cent increase in real disposable income, while other households experienced a 1 per cent increase. The single person household with no children received the greatest increase in their real disposable income from the increase in the FMW in October 2008: a 3 per cent increase. Disposable incomes of the couple with no children and single-parent allowee with one child increased by around 2 per cent as a result of the wage increase, while those of the single-parent pensioner and couple with two children increased by just over 1 per cent.

18 The disposable income figures that form the basis of the following analysis represent quarterly 'snapshots' of the interaction of wages, taxation and income transfers (as at February, May, August and November of each year). Some components of the disposable income are derived from weekly amounts (for example, wages and income support payments), others represent the weekly equivalent value of annual amounts (for example, the low income tax offset and some components of family tax benefits). The modelling assumes that all available income transfers (income support payments, family tax benefits) are taken up and that the household is paying sufficient private rent to receive the maximum rate of rent assistance, where applicable.

19 Single parents with a youngest child aged under 8, and those with a youngest child aged 8-15 who were already on payment before 1 July 2006 are eligible for Parenting Payment (Single), which is equivalent to the age pension. By contrast, single childless people, some single parents with older children and couples with and without children are generally eligible for much less generous unemployment benefits or the related Parenting Payment (Partnered).

Figure 22: Real household disposable income for selected families with one earner on the FMW



Note: Disposable incomes have been adjusted according to published changes in the CPI.

Source: AFPCS modelling; ABS, *Consumer Price Index, Australia*, December 2008, Catalogue No. 6401.0; Australian Government, *Mid-Year Economic and Fiscal Outlook 2008-09*, released November 2008.

Relativities with Henderson Poverty Line

Relativities between the disposable incomes of households with a FMW earner and conventional low-income benchmarks can be monitored by comparing the disposable incomes of the same five household types modelled above to the relevant Henderson Poverty Line (HPL).²⁰ While the HPL has never been an official measure of the lowest income necessary for an adequate standard of living, it is commonly used in Australia as an indicator of low income.

Ratio of disposable incomes for families with one earner on the FMW to the HPL

Disposable incomes relative to relevant HPLs improved slightly for households with one FMW earner following implementation of the Commission's second general wage-setting decision in October 2007 (Figure 23). Over the longer term, there has been a slight decline in the ratios for all FMW-earner household types.²¹

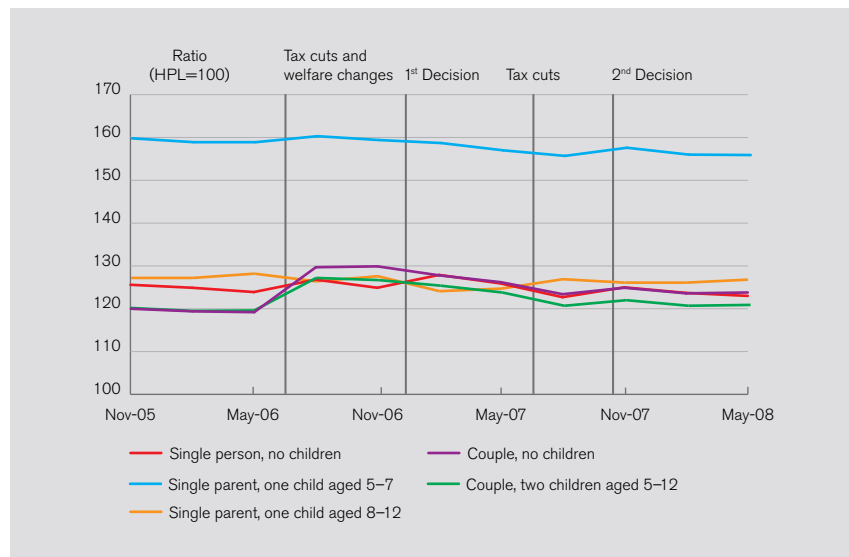
20 Henderson Poverty Lines, first established by the Henderson poverty inquiry in 1973, are based on a benchmark income required to support the basic needs of a family of two adults and two dependent children. Poverty lines for other household types are derived from the benchmark using a set of equivalence scales. The poverty lines are updated quarterly using an index of per capita household disposable income derived from ABS income and population data.

21 This trend is likely due to the fact that the HPLs are indexed to changes in average per capita household disposable income. This has tended to grow faster than either prices or wages due to ongoing decreases in average household size and increases in the proportion of households with more than one wage earner. By contrast, the disposable incomes of households with a fixed composition and only one wage earner will tend to grow at a rate consistent with increases in wages and/or prices.

Compared with the situation in August 2005, the disposable income of a FMW-earner couple with two children showed about the same relativity in May 2008, while disposable incomes of single FMW earners with and without children had declined by around 4 percentage points in relative terms. Only the couple without children still had a higher relative disposable income in May 2008 than they did in August 2005.

Throughout the period between August 2005 and May 2008, the pensioner single-parent household maintained the highest disposable income relative to the HPL, corresponding to between 156 and 160 per cent of the HPL. The disposable incomes of other modelled households ranged between 120 and 130 per cent of the relevant HPL over this time.

Figure 23: Household disposable income relative to the relevant Henderson Poverty Line for selected families with one earner on the FMW



Note: Household disposable incomes modelled and the relevant HPL include housing costs. Henderson Poverty Lines have not yet been released for the September 2008 and December 2008 Quarters.

Source: AFPCS modelling; Melbourne Institute of Applied Economic and Social Research, *Poverty Lines: Australia*, June quarter 2008.

Trends in household income, wealth and financial hardship

Research recently undertaken by Markus Hahn and Roger Wilkins of the Melbourne Institute of Applied Economic and Social Research (Melbourne Institute) for the Commission examined recent trends in household income, wealth and financial hardship among low-paid employees in Australia.²² This research found that low-paid employees were more likely than employees who were not low-paid to have low levels of household income and/or wealth. Despite this fact, the research also established that the majority of low-paid employees did not have low levels of household income and/or wealth.

Over the period from 2001 to 2006 the proportion of low-paid adult employees who were not living in a household with a low income was around five or six times as high as those who were (Table 10). Furthermore, as of 2006, the proportion of low-paid adult employees who were defined as not having low household income and low wealth was over nine times as high as those with low income and wealth.

Table 10: Percentage of adult employees who were low-paid* and had low-household income/low-wealth – 2001 to 2006

	2001	2002	2003	2004	2005	2006
<i>1. Low-income**</i>						
Low-paid and low-income	2.4	2.6	2.5	2.5	2.3	2.4
Low-paid and not low-income	13.2	13.9	14.3	13.8	13.2	14.7
<i>2. Low-income and low-wealth***</i>						
Low-paid and low-income and wealth		1.9				1.7
Low-paid but not low-income and wealth		14.6				15.4

*Low-paid employees defined as those earning less per hour than 120 per cent of the FMW, and less per week than 120 per cent of the weekly FMW.

**Low-income employees defined as those under 60% of median household income.

***Low-income and wealth employees defined as those under 60% of median household income and wealth.

Source: Hahn and Wilkins (2008), Table 16.

Hahn and Wilkins considered the location of the lowest paid in the household income distribution and found that low-paid employees are not concentrated at the lower end of the distribution. Instead, they tend to be located in the middle of the income distribution.

The study also showed a downward trend in all of the indicators of financial stress for low-paid employees over the period. The proportion of adult employees experiencing financial stress decreased for both low-paid and non-low-paid adult employees between 2001 and 2006 (Table 11).²³

22 M Hahn and R Wilkins, *A multidimensional approach to investigation of living standards of the low-paid: Income, wealth, financial stress and consumption expenditure*, report prepared for the Australian Fair Pay Commission Secretariat, 2008.

23 The Commission acknowledges that additional data would be required to determine whether or not this trend has been affected by the changing economic climate.

Table 11: Percentage of adult employees experiencing financial stress

	2001	2002	2003	2004	2005	2006
Low-paid	25.3	18.6	22.1	17.6	17.0	16.3
Not low-paid	14.1	12.0	11.5	11.0	10.6	9.0

Note: Financial stress is defined as reporting two or more indicators of financial stress.

Source: Hahn and Wilkins (2008), Table 18.

Work Incentives

This section considers financial incentives for a person who is unemployed to take up a full-time job at the FMW. It updates the indicators reported in the first *Economic and Social Indicators – Monitoring Report*. These include replacement rates, net financial gain and the proportion of earnings retained. These indicators are shown for the same household types reported in previous sections.

Overall, financial incentives for most household types appear to have strengthened, albeit only slightly. For the most part, these changes have been driven by tax cuts and, to a lesser extent, annual increases in the FMW.

Replacement rates

The replacement rate measures disposable income when out of work and fully reliant on income support as a proportion of disposable income when earning the FMW. It is a common assumption that people with higher replacement rates face a weaker financial incentive to work.

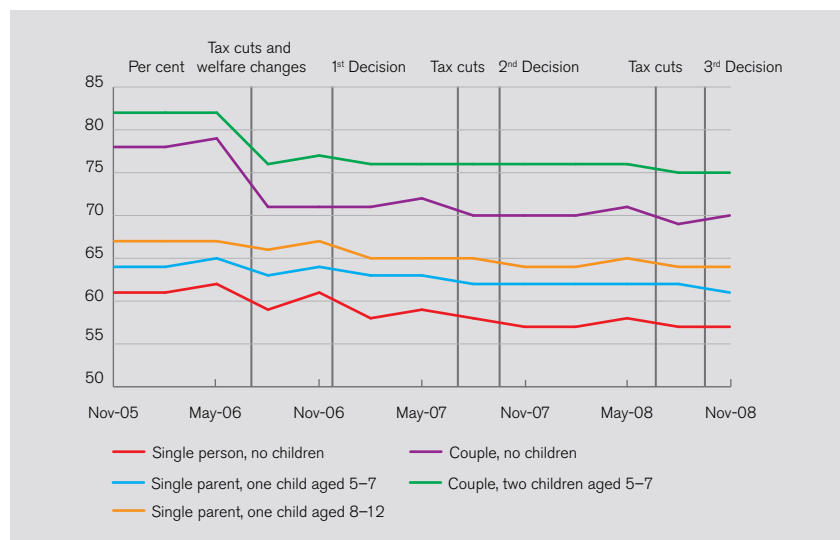
Figure 24 tracks the changes in replacement rates for the five illustrative household types²⁴ over the period from November 2005 to November 2008. It shows that replacement rates have declined slightly or remained flat for all the household types over the past year.

A single childless person now has a replacement rate of about 57 per cent, while a single-earner couple with two children has a much higher replacement rate of 75 per cent. Replacement rates for the other illustrative household types fall somewhere in between.

Replacement rates for all household types show a seasonal pattern over the course of a year. They tend to increase slightly at the May observation point (due to regular indexation of income support rates), then decline at the August and November observation points (primarily due to taxation changes in July and implementation of the FMW increase in October).

24 Changes in the Welfare to Work reforms mean that increasing numbers of single parents will be eligible only for Newstart Allowance (as opposed to Parenting Payment – single) when their youngest child reaches 8 years of age. This fifth household type has now been included in this section.

Figure 24: Income support replacement rates, households with one earner on the FMW



Note: When out of work, the single parent with one child aged 5-7 is assumed to receive Parenting Payment (single) and other household types are assumed to receive Newstart Allowance.

Source: AFPCS Modelling.

Net financial gain

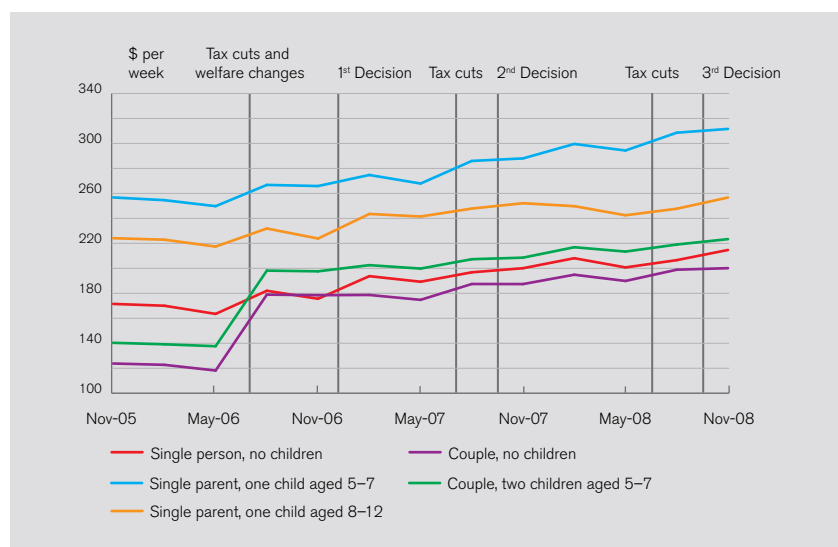
An alternative, simpler perspective on the financial incentive to take a full-time job at the FMW is provided by the net financial gain that an unemployed person would secure by taking up such a job. Figure 25 shows trends in this indicator over the period since November 2005.

Net financial gains, adjusted for CPI inflation, show an upward trend for all household types. Over the past twelve months, the largest increase has been for the single-parent pensioner household (an additional \$24 a week in real terms),²⁵ and the smallest increase for the single-parent allowance (\$5 a week). The remaining household types now earn an additional \$13 to \$16 a week, relative to their income if they were unemployed.

Most of the improvement in net financial gains derived from tax cuts in July 2008, augmented (though only marginally for a couple without children) by the October 2008 increase in the FMW.

²⁵ This is because this single parent has a more generous income test on their earnings than the other household types.

Figure 25: Real net financial gain from taking up a full-time job at the FMW, selected household types



Note: Net financial gains have been adjusted for changes in the CPI.

Source: AFPCS Modelling; ABS, *Consumer Price Index, Australia*, December 2008, Catalogue No. 6401.0.

Proportion of income retained

The third perspective on incentives to enter the workforce is provided by the proportion of a person's earnings that is effectively retained after taking account of taxation liabilities and reductions in income transfers.

Consistent with movements in the other work incentive indicators, Table 12 shows a modest but consistent increase since November 2007 in the proportion of income retained for all household types. The most pronounced increases since November 2006 are for single people, with and without children – between 4 and 6 percentage points; couple households experienced increases of around 1 percentage point over the same period.

Table 12: Net proportion of earnings retained on moving into FMW employment

Family type	November 2005	November 2006	November 2007	November 2008
Single person no children	0.33	0.35	0.38	0.39
Single parent one child, aged 5-7	0.50	0.53	0.55	0.57
Single parent one child, aged 8-12	0.42	0.41	0.46	0.47
Couple no children	0.24	0.36	0.36	0.37
Couple two children, aged 5-7	0.27	0.40	0.40	0.41

Source: AFPCS Modelling.

Summary

High inflation outcomes have offset recent increases to the FMW, leaving its real value broadly unchanged. However, after accounting for the interaction of wages, taxes and transfers, the Commission's modelling suggests that there has been continued improvement in real household disposable incomes for the households that are most reliant on a minimum-wage earner. Compared with the relevant HPLs, the disposable incomes of these households have remained stable over the period since August 2007, according to the most recent data.

The Commission's modelling also suggests that there has been continued strengthening of the financial incentives for jobless people to take up employment at the FMW, although over the past year the change has been only slight. This holds true for a number of indicators, including replacement rates, net financial gain and proportion of earnings retained.



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